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REPORT

ON THE

INTERNATIONAL DEBT (LATIN AMERICA)

OF THE

SENATE DELEGATION LED BY

SENATOR BOB GRAHAM

EXPLORATION OF THE DEBT ISSUES OF VENEZUELA, BRAZIL, AND ARGENTINA

MAY-JUNE 1988

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101ST CONGRESS
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VISIT TO SOUTH AMERICA OF THE CONGRESSIONAL DELEGATION LED BY SENATOR BOB GRAHAM

Mr. GRAHAM, from the Committee on Banking, Housing, and Urban Affairs, submitted the following

LATIN DEBT TRIP REPORT

TO THE

INTERNATIONAL FINANCE AND MONETARY POLICY SUBCOMMITTEE

Mr. Chairman, members of the Subcommittee, I led a group of Floridians to South America, May 29–June 6, 1988, to study the external debt issue. Upon receipt of post-trip information, I have prepared the following report.

OVERVIEW

Our group visited Venezuela, Brazil and Argentina, where we met with finance officers, economists, and United States and domestic bankers to discuss Latin debt issues. What we found was debt issues could not be generalized under the broad category of the "Latin debt problem."

There is a Venezuelan problem, a Brazilian problem and an Argentine problem. Substantial differences in the economies of the three countries mean that solutions to debt problems must be independent from others. No single solution can be given to the Latin debt crisis.

The debt issue is a political and economic issue and we should therefore look for political and economic solutions. The problem grows substantially worse daily as new debt is undertaken to pay interest on old debt. Severe austerity measures and the absence of investment capital to stimulate economic growth have resulted in staggering declines in the standard of living in Venezuela, Brazil

and Argentina. (Appendix I illustrates economic indicators for these countries as of June 1988.)

The United States' failure to adequately address the debt problem in these three countries is manifested in our domestic economy in several ways: decreasing exports to these countries, placing our money center banks at risk, eroding the U.S. trade position with the countries; and contributing to the U.S. budget and trade deficits.

The lack of U.S. leadership, illustrated by the passive, muddled approach taken by the Reagan Administration, affects the Latin countries adversely as well:

—Reduced standard of living and massive fiscal deficits.
—Low investment levels and reduced demand for goods in domestic markets.
—High inflation.
—Increased net export of capital.
—Reduced real income.

Politically, debt issues contribute to political tension between the United States and Venezuela, Brazil and Argentina. Our failure to resolve this issue gives Europe, Japan and the Soviet Union opportunities to increase their influence in these countries.

It appears that differences exist between the way the United States handles Latin debt compared to the Europeans. The Europeans are more flexible, acknowledging individual difficulties of these three countries. This policy engenders greater positive feelings from Venezuela, Brazil, and Argentina for the Europeans.

Country-by-Country Summary

VENEZUELA

United States banks claim disinterest in continuing their presence in Venezuela, but U.S. banks want Venezuelans to continue paying their debt. The Venezuelan bankers we met basically supported the economic position of their government. The Venezuelan Finance Ministry was proud of the fact that his nation was paying principle and interest on debt. The Finance Ministry was upset with the U.S. Government and U.S. banks, complaining that Venezuela was being treated the same as Brazil and Argentina (i.e, the United States was not making more capital available to Venezuela even though—unlike Brazil and Argentina—Venezuela has been paying its debt).

Why couldn't Venezuela be treated differently, asked the Venezuelan Finance Ministry. Venezuela intends to keep paying its debt. However, some Venezuelans have suggested deferring part of their debt payments or paying a percentage of their debt based on their export volume, like Chile.

Venezuela is facing a liquidity problem due to the declining world price of oil. Venezuela would like more capital to ease its liquidity shortage. Venezuela's domestic programs are beginning to be impacted as the nation continues to pay its debt. The Venezuelans also expressed interest in debt/equity swaps.

BRAZIL

United States banks in Brazil are pleased that the Brazilian Government is moving toward normal relations with the banking community and away from the debt moratorium imposed in 1987. Brazil's fourth round of negotiations with the international banking community put a restructuring package on the table which allowed a second International Monetary Fund (IMF) program and a Paris Club restructuring agreement.

Brazilian Finance Minister Mailson da Nobrega spoke at length to our group about the adverse impact on Brazil of its debt moratorium, including the unforeseen damage to its reputation in international financial circles. Brazil lost international credibility and suffered internal economic disfunctions by depleting its foreign exchange reserve, increasing the discount on Brazilian debt, reducing import capacity and slowing growth.

Mr. Nobrega also discussed how much time it took to negotiate with all the interested banking parties. Some 600 banks were involved in Brazil's most recent rescheduling.

ARGENTINA

United States bankers said they would continue their presence in Argentina, noting that many of them had been there a long time. However, instead of loaning new capital to Argentina as they had in the past, U.S. bankers said they would loan new capital only if it was guaranteed by the IMF or World Bank. They said Argentina needed to make economic reforms, but were unsure if politically they would be able to. United States bankers gave high marks to President Alfonsin and Finance Minister Sourrouille for trying to improve Argentina's financial position.

Agentine bankers we met with basically supported their government's debt position. They were very concerned about Argentina's high inflation rate. The Argentine bankers said they were interested in debt/equity swaps, but said their government was reluctant to allow many of them.

The Minister of Trade said Argentina was trying to strengthen its exports. Many products meant for local markets are being exported. The Deputy Minister of Finance spoke with us because President Alfonsin and Finance Minister Sourrouille were in New York City. The Deputy Minister described the economic program which Alfonsin was giving in New York at that time. Argentina is trying to make economic reforms, but also facing elections which could change economic policy.

Finally, we met with two leading economists, Roberto Aleman and Javier Gonzalez Fraga. They were candid about the economic structure of their country. They said Argentina had 13 years of triple-digit inflation, with the last four years featuring double-digit inflation per month. The economists said there had been tremendous capital flight, with local people putting their money in Argentina for seven days. Salaries are paid in dollars and the locals sell back their dollars to meet living expenses. The economists said Argentina should control inflation so capital would be invested in their country. Argentina keeps interest rates low to their creditors (Argentine banks), but makes rates high for international banks.

The economists made two final points. First, Argentina must accomplish reforms, including balancing its budget, reducing export restrictions and improving exchange rates. Second, the United States should provide its bank regulators more flexibility in regulatory and tax structure. United States rigidity does not help Argentina make economic reforms, they said.

Conclusions

The United States is losing its international leadership position and needs to reassert its fundamental commitment to international financial institutions.

The United States needs to place its domestic financial institutions on parity with European counterparts.

The United States should encourage maximum commonality and parity of treatment for Latin debt by the industrialized nations.

Old debt should be separated from the new debt by putting a cap on the basic rate of old debt.

The United States should make it easier for Third World nations to buy back their own debt in either the primary or secondary markets.

New debt is used to pay interest on previous borrowings. This concept should be re-examined.

Creditors should facilitate and help in enforcing structural reforms made by the countries.

The United States should allow a positive adjustment in the economies of debtor countries, making possible continued economic growth.

The United States should encourage a system of rewards—not penalties—in order to create incentives for better performance in each country. The United States should: increase lines of credit, encourage greater allowances for imports on the part of the developed countries, encourage additional loans from multilateral institutions for development of vital projects and provide guarantees from those institutions for new loans.

At the regulatory level, particularly through the Federal Reserve Board, closer oversight of international lending by U.S. commercial banks should occur.

In terms of new debt, an international institution should be created or an existing institution (like the World Bank) should be used to provide loan guarantees to other international institutions or private commerical institutions. This is a superior approach to get the level of funding needed in Latin America, rather than through additional international lending.

The U.S. should assign an FHA function for a loan-guarantee program with eligibility applied to Latin debt loans to particular countries, contingent on the agreement of each country to accept economic reforms that assure economic growth.

Subcommittee Initiatives

Our Subcommittee should assist in development of democracy and free enterprise in Latin America. The United States has a great opportunity to do so. The United States needs a comprehensive policy to assist the modernization of Latin America.

I recommend the following steps during the first half of 1989:

The United States should be aggressive and pragmatic in working with Latin American nations—and international organizations such as the World Bank and the IMF—to seek resolution of the debt crisis. Latin debt issues should be addressed at the 1989 Economic Summit.

The Committee should ensure that Treasury is implementing the language set forth in the 1988 Trade Act on Latin debt and debt facilities.

Congress should re-authorize United States' contributions to the IMF and World Bank so we can continue to be involved with international considerations regarding the debt problem. The international organizations should be able to plan on U.S. contributions when budgeting debt assistance for Latin countries.

The Committee should hold hearings on debt/equity swaps, such as those underway in Mexico and Brazil. One school of thought is that resale or reduction of debt servicing reduces demand on debtor countries. Furthermore, such exchanges could allow debtor nations to benefit from the write down of the loans and to create an investment climate that would encourage domestic and foreign capital for economic growth. Others contend that debt for equity swaps are generating new problems by creating inflation and stimulating financial speculation.

The Committee needs to review U.S. banking and tax regulations that are applied by U.S. regulators to Latin debt issues to assure their workability and to compare them to other international regulations.

Recommendations by Trip Participants

Members of our travel group suggested a comprehensive U.S. economic policy toward Latin America:

(A) Present stock of debt:

(1) Principal. Assist aggressively in long-term rescheduling of debt held by U.S. banks (principal stretch-out in accordance with each country's debt servicing capacity).

(2) Interest Payments. The U.S. Government would guarantee a floor of interest payments based on the cost of funds to U.S. banks.

(3) Create a "discount window" at the Treasury for a purchasing program of present debt stock. After the discounted purchase, the debtor would service debt at the discounted price.

(B) New Floor of Financial Resources:

(1) Increase the Exchange Stabilization Fund facility at Treasury to be used as bridge loans until multilateral agencies provide additional financial resources to countries adhering to the concepts laid out in this paper.

(2) Increase significantly authority for "soft lending" by Eximbank, including longer maturities and greater grace periods.

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(3) Expand the Insurance and Financing programs of OPIC, while reducing insurance premiums.

(C) Developing countries in the region that agree to be covered under these provisions must also undertake structural adjustment to foster growth of private-sector activities and to liberalize trade and foreign investment. This comprehensive agenda should include a significant amount of conditionality to assist in economic modernization of the region.

At present, Mr. Chairman, U.S. economic policies towards Latin America lack a comprehensive approach. The current approach is fractionalized and lacks a coherent vision and strategy. A comprehensive program such as the one outlined above would significantly assist the economic modernization of the region, with positive effects for U.S. national security and for U.S. private sector activities in the region.

APPENDIX I

ARGENTINA, BRAZIL, AND VENEZEULA: ECONOMIC INDICATORS

[Dollar amounts in billions]

	Gross foreign debt	Interest payments on foreign debt as a percent of exports	Inflation consumer prices (percent)	Economic growth (percent)	Exports
Table 1:					
Argentina:					
1983	$46.9	55	433.7	2.9	$7.83
1984	49.2	56	688.0	2.5	8.10
1985	50.7	50	385.4	−4.4	8.40
1986	51.7	49	81.9	5.4	6.85
1987	53.9	48	174.8	1.4	6.35
Table 2: Brazil:					
1983	93.6	42	163.8	−2.5	21.9
1984	102.0	38	215.3	5.7	27.0
1985	105.1	38	242.3	8.4	25.64
1986	111.0	40	75.5	8.0	22.39
1987	121.3	32	374.0	2.9	26.21
Table 3:					
Venezeula:					
1983	37.7	19.75	6.95	−5.6	14.57
1984	36.3	17.75	18.3	−1.4	15.97
1985	35.7	23.2	9.1	.3	14.18
1986	34.1	27.7	12.7	5.2	8.65
1987	33.3	20.8	40.3	1.3	10.49

APPENDIX II

RESPONSES TO THE SUBCOMMITTEE QUESTIONS

Mr. Chairman, when we went to Latin America, we took questions that were of interest to you and the subcommittee. We have recently received answers to these questions which I have enclosed for your review. The responses were drafted by the finance officer or economic officer in each country. These responses have been reviewed by the Treasury Department as well.

Question 1. What is the capacity of this country to carry a debt repayment schedule?

Responses:

Venezuela.—Debt carrying capacities of countries vary widely. Factors include natural resources, economic performance and macroeconomic and structural policies. Venezuela's debt service ratio of approxiamtely 35-to-36 percent was higher than the average debt service of developing countries in 1987. The key to sustainable growth and better export performance by Venezuela, and thus its ability to service and reduce its debt, is more efficient use of domestic resources in public and private sectors. Macroeconomic stabilization needs to be supported by policy reform in trade, agriculture, industry, energy and human resources.

Venezuela has a poor record of economic reform. If Venezuela implemented meaningful macroeconomic, structural and sectoral reforms it would significantly improve its ability to service its debt. Venezuela has tremendous natural resources, including 58 billion barrels of proven oil reserves. As nearly 90 percent of Venezuela's export revenues are derived from sale of oil, the debt service burden for Venezuela is affected by world oil prices. Export diversification can help reduce this dependence, which has occurred in Mexico. Venezuela's capacity to service its debt may increase in the 1990s, as important projects develop in nontraditional export areas such as aluminum, petrochemicals and gold.

Brazil.— Brazil's debt statistics are improving, as presented in Table I, which shows Brazil's external debt as a percentage of GDP and debt service ratio. External debt as a percent of GDP will fall from 48 percent of GDP in 1984 to a projected 34 percent of GDP in 1989. The debt service ratio (before rescheduling) is also improving. Brazil completed negotiations on commercial bank rescheduling in June 1988, received IMF Board approval on July 26 and a new standby agreement, and negotiated a Paris Club rescheduling last July 29.

Argentina.—In view of Argentina's wealth of natural resources, it could be fully capable of carrying a debt replacement schedule if the Argentine government implemented appropriate economic policies, and if world agricultural prices recover from depressed levels of most of the 1980s. Nevertheless, Argentina will continue to need

significant external financing over the next several years. Sources of this external financing include the IMF, the World Bank and commercial banks.

Question 2. What are the economic consequences to these countries if they make the payments? How will they handle their budgets? Will they have to divert resources which meet human needs and/or domestic and economic development?

Responses:

Venezuela.—Commercial bank lending to developing countries grew very rapidly between 1974 and 1982, increasing the total medium and long-term debt of developing countries to promote high—and unsustainable—levels of domestic growth and to finance major public investment programs. With hindsight, it is clear that lending and borrowing decisions were often imprudent and that borrowing was excessive. New funds were often channeled into low-yielding investments. Consequently, if loans had been efficiently invested, the external debt problem would have been more manageable.

The need for resources to service debt forced many countries to undertake rigorous domestic adjustments. Limited access to foreign financing meant that current account deficits had to be cut back, and that trade balances had to move strongly into surplus. The need to reduce fiscal deficits and service debt means that a higher proportion of government budgets were devoted to servicing debt. In Venezuela, debt service in 1987 amounted to 28 percent of the central Government budget.

The key to economic development (i.e., sustainable economic growth) is more efficient use of domestic resources and greater capital inflows to help finance new productive capacity. Both depend on structural reform by the debtor country.

Brazil.—Each country must choose how it will allocate its resources. Finance Minister Mailson Da Nobrega has chosen to negotiate with Brazil's official and private creditors in order to normalize Brazil's relations with the international financial community. A commercial bank financing package has been negotiated which would provide $5.2 billion in new money this year. A number of export credit agencies, including the U.S. Eximbank, are again providing financing to Brazil.

Argentina.—The prime economic consequence to Argentina of servicing its external debt is to reduce the internal financial resources available to finance investment projects needed to develop the economy. Additionally, in part because of the decreasing level of trade surpluses over the past few years (a trend reversed in 1988), Argentina must obtain new external financing if it is to meet its external debt servicing requirements. Of course, this has the side effect of increasing Argentina's total external debt and relatedly its future debt service requirements.

The true budget burden of servicing the external debt is a function of the percentage of the debt financed by domestic resources compared to the percentage financed by external loans. For example, in 1987, Argentina only financed about one-fifth of the $4 billion in debt service payments. In Argentina's case, if the bulk of its external debt obligations incurred in the years immediately prior

to 1982 were not used for investment of borrowed funds, Argentina's current debt burden would probably be more easily managed.

If economic growth is insufficient to enable the country to meet dometic budgetary goals as well as service fully its external debt, then choices must be made. To the extent that debt servicing is financed by external sources, this frees up domestic resources. In order to support sustained non-inflationary economic growth, a country must use domestic resources efficiently. This also implies domestic economic policies which improve the investment climate and encourage the return of flight capital.

Question 3. How much of the country's trade policy is driven by its debt burden? How much of the export sector is used to repay debt and to earn foreign exchange?

Responses:

Venezuela.—Venezuelan trade policy is driven by the longstanding need to assure adequate and diversified markets for its oil exports, which will remain the predominant income earner for the foreseeable future. The volatility of oil prices over the past several years has led the Venezuelan government to undertake projects to diversify its export base. The IMF estimates the total debt service ratio (debt to export earnings) at approximately 36 percent for 1987.

Brazil.—Brazil is actively promoting exports to earn hard currency in order to service its debt. In 1987, net interest payments totalled $8.8 billion compared to exports of $26.2 billion.

Argentina.—Traditionally, Argentina (like the United States) has looked inwardly for economic development. Argentina wants to increase its exports of manufactured products only when the domestic economy is in a recessionary phase. The vast bulk of Argentina's exports are agricultural products, in which Argentina has a strong comparative advantage. The Government of Argentina's policies leading towards greater trade liberalization may be largely motivated by debt repayment obligations.

While estimates vary widely, the World Bank estimates Argentina's debt service ratio in 1987 to be 54 percent.

Question 4. If these countries had no debt, would they export less and import more?

Responses:

Venezuela.—Venezuela's level of imports prior to the 1987 debt crisis was unsustainable—and the decline inevitable—because the imports were being financed by foreign borrowing beyond the potential to service debt.

With less debt burden, Venezuela might be less pressured to produce through exports the foreign exchange to service its debt. The country might also find itself able to devote more attention to investment, and if it maintained appropriate policies, it could achieve sustainable growth. The effect of such growth on imports and exports is not clear, although it would depend heavily on trade policy, exchange rates and consumer behavior.

Brazil.—Debt acts as a further stimulant to export and, unless economic growth keeps pace, can limit capacity to import. Increased growth would also affect Brazilian trade performance, although the exact influence of such economic expansion on imports

and exports would depend heavily on factors such as trade policy, exchange rates and consumer behavior.

Argentina.—It is difficult to predict whether Argentina would export less and import more if it had no external debt. Some of the factors involved are: exchange rate policy, terms of trade, trade policies, inflation and other macroeconomic policies. There are clear signs that the Argentine government is moving now to liberalize the trade sector. These policies, which may be largely motivated by pressures generated by external debt repayment obligations, should lead to significant increases in both exports and imports.

Question 5. What are these nations' predictions of their ability to carry debt?

Responses:

Venezuela.—In 1987, Venezuela signed a 14-year public sector rescheduling agreement. Most rescheduling agreements are negotiated with both debtors and creditors aiming to ensure continued servicing of the debt. Venezuela presumably would not have accepted the agreement if it did not think the rescheduling would enable it to carry its debt. An increased inflow of money—through foreign direct investment, bond issues, long-term project finance or increased trade lines—could enhance Venezuela's financial position. The Government of Venezuela is encouraging the flow of new money on all these fronts via various initiatives.

Brazil.—Brazil can service its debt under the terms of its recent debt reschedulings.

Argentina.—The Argentine Government maintains that Argentina is in position to service regularly out of its own resources about half of its annual external debt service payments. Argentina negotiates with its creditors to reschedule external debt with the goal of continuing to service its debt commensurate with its ability to do so.

Question 6. How can the debt burden be handled?

Responses:

Venezuela.—The Venezuelan Government is encouraging the inflow of new money by various mechanisms. It has encouraged direct foreign investment by liberalizing investment regulations, particularly for large projects in high-priority sectors which generate foreign exchange. The government is attempting to return to the international bond market. Venezuela is extending repayment terms for trade credit lines. It is reviewing the possibility of utilizing some official credit programs such as the Commodity Credit Corporation.

Brazil.—Brazil can service its debt under the terms of its recent debt reschedulings.

Argentina.—Argentina's debt burden can best be handled if the Argentine economy achieves a continued period of self-sustained growth. Full implementation of government policies to reform the role of the state, restructure the economy and integrate the Argentine economy into world markets—combined with continued external financing—offer the best hope for handling the debt burden.

Question 7. What is the role of the private banking sector?

Responses:

Venezuela.—Commercial banks have traditionally been the major suppliers of credit to Venezuela. More than 80 percent of Venezuela's external debt is owed to private commercial banks. Given the refusal of Venezuela to avail itself of resources from the IMF or IBRD (due to conditionality), it is likely that Venezuela will look to commercial banks to play a predominant role in meeting Venezuela's debt needs.

Brazil.—Private commercial banks hold approximately two-thirds of Brazil's debt. They play an important role in Brazil for trade and finance.

Argentina.—The Argentine Government sees the role of private banks as suppliers of needed financing for debt servicing, trade financing and, in the longer term, financial lines.

Question 8.—Are the countries treated differently by U.S. banks versus foreign banks?

Responses:

Venezuela.—United States banks hold more than one-third of the approximately $24 billion of Venezuelan public debt outstanding. U.S. banks continue to participate in concerted lending packages at a level proportional to the banks' exposure to the country in the designated base year. International voluntary lending occurs subject to discretion of each bank, with U.S. banks more likely to remain involved in Latin America due to its proximity and market for U.S. exports there.

Brazil.—United States and other foreign banks work together in their dealings with Brazil. The commercial bank advisory committee is made up of 14 banks representing the spectrum of Brazil's creditors. The committee includes representatives from United States, French, German, British, Japanese and Canadian banks, among others. Each bank involved in Brazil continues to participate in concerted lending packages at a level proportional to its exposure to Brazil in the designated base year. At the same time, each bank engages in voluntary lending at its discretion. The proximity of Latin America and its potential as a market for U.S. exports make it more likely that U.S. banks will remain engaged in the region.

Argentina.—European and Japanese banks seem to be primarily interested in maintaining trade lines. U.S. banks, on the whole, participate in lending packages commensurate with the level of their exposure in the country. Several U.S. banks have longstanding operational ties to Argentina and are more likely to continue their presence in the country.

Question 9. If we give Latin debtor nations additional assistance, would it be tied to increased assistance for trade, like increased Japanese imports?

Responses:

Venezuela.—USAID has no program in Venezuela. U.S. Eximbank lends to Venezuela, and Venezuela is required by Eximbank to tie its financing to U.S. procurement. With regard to the Japanese program for Latin America, we understand that this assistance will not be tied to procurement from Japan.

Brazil.—The United States provides financing to Brazil through the Eximbank and the Commodity Credit Corporation, which are required by law to tie their financing to U.S. procurement.

Argentina.—USAID does not have a program in Argentina. Eximbank does provide financing tied to U.S. procurement.

Question 10. Are foreign banks lending more or less because they have to hold higher reserves? Should we reach multilateral agreements with all banks involved in a country?

Responses:

Venezuela.—Generally, bank regulators have made a start toward greater international convergence of capital measurement and capital standards, adopted July 1988 by members of the Bank for International Settlements. This is a first step, but in many countries, including the United States, regulators allow individual banks to set the levels of their own general loan loss provisions, subject to prudential standards. Some banks many choose to have higher levels than others, based on perceptions of overall risk.

However, when banks decided to hold reserves against specific countries, or regulators mandate such reserves they no longer count as capital. They are subject to differing regulatory, accounting, and tax treatment depending on the nationality of the bank. In addition, different categories of loans may be treated differently, depending on how they are being serviced. While some convergence of reserving practices may take place, it is unrealistic to assume harmonized treatment, given the differing national rules involved. Lending decisions are based on assessment of risk, credit worthiness repayment possibilities and profitability.

Brazil.—Bank regulators have made a start toward greater international convergence of capital measurements and capital standards, evidenced by an agreement adopted July 1988 by members of the BIS. This is a first step toward multilateral standards, but in countries such as the United States (and others), regulators allow individual banks to set the levels of their own general loan loss provisions, subject to prudential standards. Some banks may choose to hold higher levels of reserves than others, based on perceptions of overall risk and the bank's capital position.

When a bank assigns some portion of its reserves to a particular country or group of countries—or when regulators mandate such reserves—those funds no longer count as capital for the bank. Country-specific reserves are subject to differing regulatory accounting and tax treatment depending on how they are being serviced. While some convergence of reserving practices may take place, it is unrealistic to assume harmonized treatment. Lending decisions are based on assessment of risk, creditworthiness, repayment possibilities and profitability.

Argentina.—Some foreign banks, such as European banks, on the whole carry loan loss reserves at higher levels than U.S. banks. While the level of loan loss reserves held by a bank is one factor determining its lending policy, ultimate lending decisions also depend on each bank's existing lending portfolio to a given country, the mix of its remaining portfolio, and its assessment of risk and profitability. Other regulatory, tax and accounting considerations may also apply.

Question 11. What should the U.S. Government and banks be doing?

Responses:

Venezuela.—The United States and commercial banks should continue a flexible case-by-case approach which stresses economic adjustment by debtors and supports such adjustment through adequate financial support. All debtors stand to benefit from the current strategy. The menu of available options which are voluntary and market-based, has been expanded to facilitate debtor and creditor ability to negotiate workable financing packages.

Brazil.—The U.S. Government and private commerical banks should support countries which are working with the IMF and World Banks and are undertaking substantial structural adjustments in order to achieve sustainable growth and development and to service external debt. Now that it has committed itself to structural reforms and is engaged positively with the international financial community, Brazil is such a case.

Argentina.—The United States and commercial banks should continue to support and encourage Argentine Government efforts to restructure and reform the Argentine economy in the context of our current case-by-case growth-oriented debt strategy. This flexible approach permits lenders and creditors to select from an expanding menu of voluntary, market-based options to include in negotiated financing packages.

Question 12. If we provide debt relief, do they think it should be conditional to whether they implement economic reforms from the World Bank or the IMF?

Responses:

Venezuela.—The only credible form of debt reduction is that which is voluntarily agreed upon by individual debtors and creditors within the context of the market. Mechanisms for involuntary general debt relief or forgiveness would hinder debtor access to future credit (even short-term trade lines), could distract debtors and creditors alike from the difficult but fundamental economic adjustment talks, and risk encouraging counterproductive debt repudiations aimed a maximizing the so-called "benefits" of forgiveness. Moreover, such mechanisms could entail a shift of risk on private sector loans to the public sector and could require major expenditures of taxpayer money.

The Venezuelan government is currently of the view that no international financial transaction should be conditioned on economic reform, which is a sovereign matter. While it is recognized by some Venezuelan policing that economic reforms are necessary, they maintain that the timing and pace of such reforms is an internal matter. As a result, even IMF and World Bank funds, which are conditional on economic policy reforms, have not been available to Venezuela.

Brazil.—Commercial bank reschedulings, which can involve some measure of debt reduction, are normally conditioned on IMF adjustment programs. Such linkage to economic reforms provides a basis for credible debt reduction in voluntary, market-based agreements between debtors and creditors. The rescheduling negotiated by Brazil within the Paris Club on July 29, 1988, adhered to this framework.

Argentina.—Debt relief, per se, is no panacea. Reduction in debt and debt servicing must be voluntarily worked out between debtors and creditors in order to ensure the viability of the flow of future

voluntary financing needed for Argentina to develop its economy. Appropriate economic policies are also necessary if debtor countries are to establish the creditworthiness needed for voluntary lending. Any U.S. actions in support of Argentina should be conditioned on whether the government implements needed economic reforms and continues to work together with the IMF and the World Bank.

DELEGATION OF THE U.S. SENATE

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